

ORIGINAL



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MEMORANDUM

TO: Docket Control

FROM: Steven M. Olea
Director
Utilities Division

DATE: October 26, 2011

Arizona Corporation Commission

DOCKETED

OCT 26 2011

DOCKETED BY	
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RE: STAFF REPORT FOR GLOBAL UTILITIES'¹ AND AFFILIATED HOLDING COMPANIES'² JOINT APPLICATION FOR AUTHORITY TO ISSUE ADDITIONAL EQUITY AND TO EFFECT ANY NECESSARY CORPORATE RE-ORGANIZATION (DOCKET NOS. W-20446A-11-0124, SW-20445A-11-0124, SW-20422A-11-0124, W-02442A-11-0124, W-01732A-11-0124, W-03720A-11-0124, W-01212A-11-0124, W-02451A-11-0124, W-02450A-11-0124, SW-20403A-11-0124, W-20495A-11-0124, SW-20494A-11-0124)

Attached is the Staff Report for the Global Utilities' and their affiliated holding companies' joint application for authority to issue additional equity and reorganize. Staff recommends approval.

Any party who wishes may file comments to the Staff Report with the Commission's Docket Control by 4:00 p.m. on or before November 2, 2011.

SMO:JCM:red

Originator: Juan C. Manrique (Gordon Fox)

Attachment: Original and thirteen copies

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2011 OCT 26 P 2:32
AZ CORP COMMISSION
DOCKET CONTROL

¹ Global Water – Santa Cruz Water Company, Global Water – Palo Verde Utilities Company, Hassayampa Utility Company, Inc., Global Water – Picacho Cove Water Company, Global Water – Picacho Cove Utilities Company, CP Water Company, Willow Valley Water Co., Inc., Water Utility of Northern Scottsdale, Inc., Valencia Water Company, Inc. – Town Division, Valencia Water Company, Inc. – Greater Buckeye Division, Water Utility of Greater Buckeye, Inc., Water Utility of Greater Tonopah, Inc. and Balterra Sewer Corp.

² Global Water Resources, Inc., Global Water, L.L.C., and West Maricopa Combine, Inc.

SERVICE LIST FOR: GLOBAL UTILITIES
DOCKET NOS. W-20446A-11-0124 ET AL

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**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

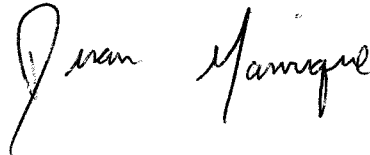
**GLOBAL UTILITIES AND AFFILIATED HOLDING COMPANIES
DOCKET NOS. W-20446A-11-0124, SW-20422A-11-0124,
W-01732A-11-0124, W-01212A-11-0124, W-02450A-11-0124,
W-20495A-11-0124, SW-20445A-11-0124, W-02442A-11-0124,
W-03720A-11-0124, W-02451A-11-0124,
SW-20403A-11-0124, SW-20494A-11-0124**

APPLICATION TO ISSUE ADDITIONAL EQUITY AND REORGANIZE

OCTOBER 26, 2011

STAFF ACKNOWLEDGMENT

The Staff Report for Global Utilities and Affiliated Holding Companies, (Docket Nos. W-20446A-11-0124, SW-20422A-11-0124, W-01732A-11-0124, W-01212A-11-0124, W-02450A-11-0124, W-20495A-11-0124, SW-20445A-11-0124, W-02442A-11-0124, W-03720A-11-0124, W-02451A-11-0124, SW-20403A-11-0124, SW-20494A-11-0124) is the responsibility of the Staff members listed below. Juan C. Manrique is responsible for the financial analysis.

A handwritten signature in cursive script, reading "Juan Manrique". The signature is written in dark ink and is centered above the printed name.

JUAN C. MANRIQUE
PUBLIC UTILITIES ANALYST I

**EXECUTIVE SUMMARY
GLOBAL UTILITIES
DOCKET NOS. W-20446A-11-0124, ET AL**

On March 18, 2011, Global Utilities¹ and their affiliated holding companies² filed a Joint Notice of Intent with the Arizona Corporation Commission ("Commission") requesting authorization under Arizona Administrative Code ("A.A.C.") R14-2-803 for the issuance of additional equity and any necessary corporate reorganization. Additionally, Global requests removal of a series of conditions previously imposed on it.

Decision No. 70980, which authorized Global's initial public offering ("IPO"), mandated twelve conditions. Global has requested that all of these conditions be removed as unnecessary due to the IPO being completed. Staff agrees that most of these conditions should be removed. However, Staff concludes that a small number of these conditions should remain in effect either as stated or with slight modifications as follows:

- A) Condition No. 5 prohibits recovery, in any rate proceeding, of the costs incurred to implement the proposed transactions, including rate case cost of capital calculations. While Staff does not object to the removal of this condition, Staff notes that cost of equity authorizations already provide for recovery of the transaction costs. Therefore, it is unnecessary to contemplate any of these costs separately from the cost of equity in a rate case.
- B) Condition No. 6 requires an equity improvement plan that results in at least 30 percent equity by December 31, 2015. Staff acknowledges that Global has filed an equity improvement plan in the previous docket; however, contrary to Global's assertion that the condition has been satisfied, Global's plan has not yet resulted in achievement of a capital structure with at least 30 percent equity. Staff recommends that the condition be modified to require that Global file an equity improvement status and update plan on an annual basis demonstrating Global's progress toward and explaining how it intends to reach at least 30 percent equity in its capital structure by December 31, 2015. This annual requirement should remain until U.S. Global reaches 30 percent equity.
- C) Condition No. 7 requires that Global continue to maintain the location of its books and records in Maricopa County, Arizona. Staff agrees with Global that maintaining the books in Maricopa County is unnecessary. However, Staff

¹ Global Water – Santa Cruz Water Company, Global Water – Palo Verde Utilities Company, Hassayampa Utility Company, Inc., Global Water – Picacho Cove Water Company, Global Water – Picacho Cove Utilities Company, CP Water Company, Willow Valley Water Co., Inc., Water Utility of Northern Scottsdale, Inc., Valencia Water Company, Inc. – Town Division, Valencia Water Company, Inc. – Greater Buckeye Division, Water Utility of Greater Buckeye, Inc., Water Utility of Greater Tonopah, Inc. and Balterra Sewer Corp. (collectively, "Global Utilities").

² Global Water Resources, Inc., Global Water, L.L.C., and West Maricopa Combine, Inc. (together with Global Utilities, "Global").

recommends requiring Global to make all books and records available to Staff within Maricopa County, Arizona, at Staff's request.

- D) Condition No. 11 requires that all Global affiliates charge the lower of fully-allocated cost or market price whenever goods, products or services are sold or provided to a Global Utility. It also requires that any Global Utility will charge the higher of fully-allocated cost or market price whenever goods, products or services are sold or provided by a Global Utility to an affiliate. It further states that Global Utilities and affiliates will, on a continuing basis, retain market research information used to determine the market price for goods or services until the completion of the Global Utility's subsequent rate case.

The Company argues that costs of goods, products and services provided by affiliates do not require a special condition, and should be evaluated based on standard ratemaking principles. Staff recommends retaining these conditions. These transfer pricing practices follow recognized ratemaking guidelines; however, guidelines do not provide the definitive ratemaking treatment resulting from a Commission directive. Further, Staff opposes removal of the requirement to retain supporting market research information.

Staff concludes that Global's requested authorization for equity issuances is within its corporate powers, is compatible with the public interest, will not impair its ability to provide services and is consistent with sound financial practices.

Staff recommends approval of Global's proposed equity issuance authorizations and approval of Global's request to remove the conditions imposed under Decision No. 70980, except as discussed above.

Staff further recommends that the Commission grant approval for any corporate reorganization, limited to the formation of holding companies or affiliates that may be necessary or appropriate in conjunction with the issuance of additional equity, subject to U.S. Global remaining as a holding company with effective oversight and control over Global Utilities.

Staff further recommends authorizing Global to engage in any transactions and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that Global file with Docket Control, as a compliance item in this matter, copies of any documents related to the issuance of stock as outlined in this application within 60 days of the execution of any transaction authorized herein.

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INTRODUCTION

On March 18, 2011, Global Utilities¹ ("Global" or "Company") and their affiliated holding companies² filed a Joint Notice of Intent with the Arizona Corporation Commission ("Commission") requesting authorization under Arizona Administrative Code ("A.A.C.") R14-2-803 for the issuance of additional equity and any necessary corporate reorganization. Additionally, Global requests removal of a series of conditions previously imposed on it.

BACKGROUND

Global is part of Global Water Resources, Inc. ("U.S. Global") which owns and operates a series of public service corporations across the U.S. including Arizona. U.S. Global is privately-held and is substantially-owned (approximately 48.1 percent) by GWR Global Water Resources Corp. ("Canadian Global"). Canadian Global's shares are publicly traded on the Toronto Stock Exchange using the ticker symbol GWR. No shareholder other than Canadian Global currently owns more than 25 percent of U.S. Global. U.S. Global is the parent of the Global Utilities.

COMPLIANCE

A check of the Utilities Division Compliance Database indicates that there are currently no delinquencies for Global Utilities.

REORGANIZATION

Requirements

A.A.C. R14-2-803(A) states, "Any utility or affiliate intending to organize a public utility holding company or reorganize an existing public utility holding company will notify the Commission's Utility Division in writing at least 120 days prior thereto." Decision No. 58063, dated November 3, 1992, states that a public utility holding company increasing or decreasing its financial interest in an affiliate would be considered a reorganization and therefore would be subject to A.A.C. R14-2-803. A.A.C. R14-2-803(A) directs a utility to include certain information related to the reorganization in its notice of intent. Staff concludes that the information provided by Global in the application and supplemented by further discovery submitted to Utilities Division Staff ("Staff") is satisfactory.

¹ Global Water – Santa Cruz Water Company, Global Water – Palo Verde Utilities Company, Hassayampa Utility Company, Inc., Global Water – Picacho Cove Water Company, Global Water – Picacho Cove Utilities Company, CP Water Company, Willow Valley Water Co., Inc., Water Utility of Northern Scottsdale, Inc., Valencia Water Company, Inc. – Town Division, Valencia Water Company, Inc. – Greater Buckeye Division, Water Utility of Greater Buckeye, Inc., Water Utility of Greater Tonopah, Inc. and Balterra Sewer Corp. (collectively, "Global Utilities").

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A.A.C. R14-2-803(B) states that “[t]he Commission will, within 60 days from the receipt of the notice of intent, determine whether to hold a hearing on the matter or approve the organization or reorganization without a hearing.” A hearing would provide a full record with respect to this proposed reorganization.

A.A.C. R14-2-803(C) provides that “the Commission may reject the proposal if it determines that it would impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service.”

Decision No. 67240 (September 15, 2004) mandated that “Palo Verde Utilities Company, LLC, Santa Cruz Water Company, LLC, and Global Water Resources, LLC, must notify the Commission of any proposed change in the ownership of their respective membership interests (including transfer or additional memberships), prior to execution, through filing of a Notice of Intent (which indicates the filing is made pursuant to the Decision in this proceeding). Once the Notice of Intent has been filed, the Commission may initiate a proceeding within 60 days to determine approval. If no action is initiated within 60 days after filing, the proposed transaction is permitted to proceed without approval.” This condition was affirmed in Decision No. 67830 (May 5, 2005).

Global has waived the aforementioned time limits as defined in the A.A.C., as well as those in the referenced Commission Decisions.

Capital Structure

Staff calculated U.S. Global’s capital structure as of December 31, 2010, to consist of 3.8 percent short-term debt, 38.1 percent long-term debt, 3.8 percent equity, 33.8 percent Advances In Aid of Construction and 20.6 percent Contributions In Aid of Construction. Given U.S. Global’s highly leveraged capital structure, any reasonable amount of additional equity infusions will assist it in moving toward and maintaining a balanced capital structure. An improvement in U.S. Global’s equity position would enhance its ability to provide equity to the Global Utilities.

CONDITIONS

Decision No. 70980, which authorized Global’s initial public offering (“IPO”), mandated twelve conditions as follows:

- 1) The corporate restructuring, the IPO or the private placement and the reorganization must take place by April 30, 2011.
- 2) The equity issued, transferred or sold by the new Global parent using private placement or an IPO must not exceed 49.9 percent of the voting common stock.

- 3) If Global decides to issue equity exceeding 49.9 percent of the voting common stock, or issue equity in any other manner other than the private placement or IPO discussed in [the March 19, 2009 Amended] Staff Report and the Staff Report filed February 4, 2009, it should file a new application and a hearing may be required.
- 4) Global Utilities will continue to maintain their business headquarters and fully-operational field, billing and complaint offices in Arizona.
- 5) Global Utilities will not recover, in any rate proceeding, the costs incurred to implement the proposed transactions. This includes rate case cost of capital calculations.
- 6) Global will produce, file in this docket, and implement, within 90 days of the decision in this matter, an equity improvement plan which results in at least 30 percent equity by December 31, 2015.
- 7) Global shall continue to maintain the location of its books and records in Maricopa County, Arizona.
- 8) Upon completion of the IPO or private placement and any subsequent series of equity issuances approved in this docket, Global will file information in this docket regarding the number of shares, the price, and the cost of each issuance. This will be filed within 60 days of each issuance.
- 9) Before a Global Utility shares with affiliates, or other entities, information made available to the Utility solely by virtue of the company/customer relationship, such as billing information and services received by a customer, the Global Utility shall file and receive approval of a tariff setting forth appropriate customer notification procedures to inform customers about the sharing. Customer information prohibited from disclosure does not include a customer's name, address or service location, and telephone number.
- 10) No Global affiliate shall perform services for, receive services from or use any assets of the Global Utilities without a written contract with the Global Utility(ies) concerning such services or assets and that until completion of the first Global Utility rate case, such contracts must be filed in this docket.
- 11) All Global affiliates shall charge the lower of fully-allocated cost or market price whenever goods, products or services are sold or provided to a Global Utility. The Global Utilities will charge the higher of fully-allocated cost or market price whenever goods, products or services are sold or provided by a Global Utility to an affiliate. Further, the Global Utilities and Global affiliates will retain market

research information used to determine the market price for goods or services until the completion of the subsequent rate case.

- 12) Global Water Resources Inc.'s Board of Directors shall establish procedures to review transactions between affiliates and file these procedures in this docket.

Global requests removal of all of these conditions claiming that they are unnecessary due to completion of the IPO. Staff agrees that most of these conditions should be removed. However, Staff concludes that a small number of these conditions should remain in effect either as stated or with slight modifications as follows:

- A) Condition No. 5 prohibits recovery, in any rate proceeding, of the costs incurred to implement the proposed transactions, including rate case cost of capital calculations. While Staff does not object to the removal of this condition, Staff notes that cost of equity authorizations already provide for recovery of the transaction costs. Therefore, it is unnecessary to contemplate any of these costs separately from the cost of equity in a rate case.
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CONCLUSION AND RECOMMENDATIONS

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Staff further recommends that the Commission grant approval for any corporate reorganization, limited to the formation of holding companies or affiliates that may be necessary or appropriate in conjunction with the issuance of additional equity and subject to U.S. Global remaining as a holding company with effective oversight and control over Global Utilities.

Staff further recommends authorizing Global to engage in any transactions and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that Global file with Docket Control, as a compliance item in this matter, copies of any documents related to the issuance of stock as outlined in this application within 60 days of the execution of any transaction authorized herein.

FINANCIAL ANALYSIS

	[A] ¹ <u>12/31/2010</u>	
Short-term Debt	\$11,702,000	3.8%
Long-term Debt	\$117,361,000	38.1%
Common Equity	\$11,618,000	3.8%
Advances in Aid of Construction	\$104,043,000	33.8%
Contributions in Aid of Construction	\$63,360,000	20.6%
Total Capital	\$308,084,000	100.0%

¹ Column [A] is based on U.S. Global's consolidated financial information for the year ended December 31, 2010.